

August 21, 2015

Expert Advisory Panel – FSCO/FST/DICO Mandate Reviews
Ministry of Finance
Financial Institutions Policy Branch (FIPB) & Income Security & Pension Policy Division
Frost Building North, Room 424
95 Grosvenor Street, 4th Floor
Toronto, ON
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Sent by email to: FIPBmandatereview@ontario.ca

Dear Sirs:

RE: FAIR Canada Comments on Review of Mandate of FSCO

Further to our meeting with the Expert Advisory Panel (the “Panel”) on Wednesday, August 12, FAIR Canada would like to provide in writing to the Panel a brief summary of the points we raised. Our comments respond to the issues raised in the Ministry of Finance’s Consultation Paper issued April 21, 2015 (the “Consultation Paper”) and in response to the key issues that the Panel must address further to its Terms of Reference in relation to the Financial Services Commission of Ontario (“FSCO”).

FAIR Canada is a national, charitable organization dedicated to putting investors first. As a voice of Canadian investors, FAIR Canada is committed to advocating for stronger investor protections in securities regulation. Visit www.faircanada.ca for more information.

I. FAIR Canada’s Recommendations in Response to Questions Regarding the Mandate of FSCO

1. Revise the Mandate of FSCO

FAIR Canada is of the view that the mandate or purposes of FSCO need to be revised and made clear. **The mandate should be to foster a fair and efficient financial services marketplace (or a well-functioning market for financial services) and robust protection of consumers.**

We note that support for the explicit legal inclusion of financial consumer protection in the mandate of FSCO can be found in the OECD’s G20 High-Level Principles on Financial Consumer

Protection.¹ It would also be similar to the mandate of securities regulators. Consumers of insurance-related products deserve no less.

A “dual” mandate (fostering a fair and efficient market / consumer protection) should be balanced through three principles:

- (i) Market efficiency is a necessary, but insufficient, condition for achieving fairness and consumer protection;
- (ii) Market efficiency cannot be achieved without consumer confidence in the market; and consumer confidence can only be achieved when consumers feel they are treated fairly and are adequately protected; and
- (iii) Consumer protection is not achieved at the expense of market efficiency. Rather, robust consumer protection is an essential building block to a fair and efficient financial services marketplace and confidence in that marketplace.

Striving to achieve the dual mandate should lead to a “strong financial services sector”. However, we do not think that a “strong financial services sector” should be the goal since that goal could very well conflict with both appropriate consumer protection and an efficient marketplace.

2. Need Effective Consumer Stakeholder Engagement

Effective stakeholder engagement is essential for FSCO to succeed. That engagement is necessary in all areas that FSCO oversees. It should be achieved through (a) a consumer advisory panel, along with (b) consumer representation in the revised governance framework for FSCO.

Consumers need to be represented in the policy-making process and this is currently not being done in any adequate way by FSCO. We refer you to our 2011 submission to FSCO regarding its draft Statement of Priorities wherein we recommended that:

- (i) FSCO should undertake a specific initiative to obtain the views of financial consumers in order to understand their concerns and be accountable to their interests; and
- (ii) as a means of doing so, FSCO should strengthen the Consumer Advisory Committee which FSCO created in 2001.²

¹ OECD’s High Level Principles on Financial Consumer Protection, October 2011, available online at <http://www.oecd.org/daf/fin/financial-markets/48892010.pdf>

² FAIR Canada letter to Phil Howell of FSCO dated June 6, 2012 at page 9, available online at <http://faircanada.ca/wp-content/uploads/2011/01/FAIR-Canada-submission-re-FSCO-Draft-Statement-of-Priorities.pdf>.

We reiterated the importance of obtaining the views and perspectives of the consumer when developing policy in our 2012 submission to FSCO in response to its draft Statement of Priorities.³

As noted by PIAC in a February 2014 submission to the Department of Finance: “Although financial products/services are of fundamental importance to most Canadians, Consumer engagement on financial issues is low. This is because Canadians do not generally have the resources necessary or the proper channels through which to input into the financial regulatory process. Financial products/services, and regulation which govern them, are beyond the realistic grasp of most people...”⁴

FAIR Canada strongly supports provisions for an independent statutory consumer advisory panel that is appropriately funded and afforded a broad mandate to represent the interests of Canadian financial consumers for the areas FSCO oversees, in particular insurance. We have made similar representations to governments and regulators regarding the cooperative capital markets regulator.

Financial consumers need a mandated seat at the table and adequate funding to actively and properly represent consumer interests on financial matters. This is sorely lacking in the insurance sector. There is a strong need for consumer representation to be hard-wired into the process in order to have an effective policy-making process.

In addition, FAIR Canada strongly recommends the inclusion of financial consumer interests in the governance structure of FSCO, whether that be a board of directors or commissioners. There should be included, on the board or amongst the commissioners, individuals who will represent the interests of financial consumers. The appointment of qualified people whose body of work is known to reflect and foster the interests of financial consumers would be in the public interest.

³ See FAIR Canada’s letter to FSCO dated June 6, 2012 at page 13-14, available online at <http://faircanada.ca/wp-content/uploads/2011/01/120606-FAIR-Canada-Submission-re-FSCO-Draft-Statement-of-Priorities.pdf>.

⁴ Canada’s Financial Consumer Protection Framework: Consultation Paper, Comments of the Public Interest Advocacy Centre, dated February 28, 2014 at page 65-66, available online at <http://www.piac.ca/our-specialities/piac-submission-to-canadas-financial-consumer-protection-framework-consultation-paper/>.

3. FSCO's Role

Regulation of Solvency

Given OSFI's expertise and the limited resources of FSCO, FSCO should continue to have responsibility for the regulation of market conduct but not the regulation of solvency for insurance companies. This could be better done by OSFI.

Regulation of Segregated Funds

The Ontario Securities Commission should regulate segregated funds in light of the following:

- (i) the expertise of the Ontario Securities Commission in regulating complex investment products;
- (ii) the basic principle that consumers should receive a similar level of protection in respect of their investments and advice related to those investments regardless of which sector of the financial industry the product or sale originates from; and
- (iii) the basic principle that like products should be regulated in like manner so that consumers have good outcomes.

If for political reasons this is not possible, then harmonization of the regulatory framework is needed so that regulatory requirements are substantially the same: the advice provided by life insurers, managing general agencies and life insurance agencies and their life insurance agents on the insurance side should be at the same standard as that required of dealers, advisers and their registered representatives on the securities side; relationship disclosure requirements, cost and performance disclosure requirements for insurance products with an investment component and point of sale requirements should all be similar. This is especially true since the access point for the sale of these products is often the same individual who is dually licensed, and can even involve investment in the same mutual fund (with a 'wrap' product). We note that the International Monetary Fund's 2014 Report assessing Canada's performance of the Insurance Core Principles made several recommendations regarding Principle 18: Intermediaries and Principle 19: Conduct of Business, including recommendations for reform where enforceable rules are lacking. Those recommendations need to be implemented.⁵

⁵ <http://www.imf.org/external/pubs/ft/scr/2014/cr1472.pdf>

FAIR Canada's letters to FSCO on their product suitability reviews of life insurance agents are attached hereto as Appendix A.⁶

4. Ability to Ensure Compliance Hampered by Existing Framework of Laws and Regulations

While the purpose of the mandate review by the Panel is not to review the legislation or regulations enforced by FSCO, the ability of FSCO to ensure compliance with existing laws (for example, adequate supervision of insurance agents) is hampered by the existing state of the laws and regulations. Insurers have a legal duty to ensure that their sponsored life insurance agents comply with applicable regulations and that their agents are suitable to be licensed as agents. However, in practice, life insurers are unable to fulfill this duty with any rigour because most life insurance agents no longer work directly for an insurer.

Similarly, how can FSCO adequately supervise the market conduct of insurance if it has limited powers regarding the review of products in its marketplace? Unlike securities regulators, FSCO does not review prospectuses before products are introduced into the marketplace. Therefore, a product can be marketed and advertised in Ontario without it having been vetted by FSCO; and consumers may purchase the product, not knowing that it may not provide what is advertised. This is not in the consumer interest.

We support the IMF's recommendations regarding ICP 19: conduct of business rules: "Empowering FSCO to issue enforceable rules on product development and promotion as well as require insurers and intermediaries to conduct needs analysis before providing advice and meet policy servicing obligations."

5. Consumer Redress Process for Financial Consumers Needs Reform

FAIR Canada recommends that the G20 High-Level Principles on Financial Consumer Protection, including Principle 9, Complaints Handling and Redress, needs to be adhered to. In particular, such a system should be "... accessible, affordable, independent, fair, accountable, timely and efficient. Such mechanisms should not impose unreasonable cost, delays or burdens on consumers."⁷ Currently, if consumers have a complaint about a segregated fund and also about other investments in their investment portfolio, they must take their segregated fund complaints to OLHI but their securities related complaints to OBSI. However, OLHI may not have the jurisdiction to handle the complaint since only insurance companies, not managing general agencies or individual insurance agents, participate in OLHI. If the complaint relates to the insurance agent (or "advisor")'s activities, it will likely not fall within OLHI's mandate.⁸ Thus, individuals too often must deal with two different ombudsmen about complaints relating to

⁶ We wrote two letters to FSCO regarding the Product Suitability Reviews of Life Insurance Agents, one dated [October 10, 2013](#) and one dated [September 24, 2014](#).

⁷ See Principle 7 of the G20 High-Level Principles on Financial Consumer Protection, at page 7.

⁸ See the second (and recent) independent review of OLHI which discusses this serious gap in redress for consumers using OLHI at Robert Wells, "Independent Review Report" prepared for OmbudService for Life & Health Insurance, available online at <http://www.olhi.ca/downloads/pdf/Independent%20-eview-Report-OLHI.pdf>.

advice given by a single “financial advisor” who is dual-licensed (as an insurance agent and registered to sell mutual funds and/or other securities) and sold them investment products some of which are securities and some of which are insurance-regulated products. This makes little sense, especially since OLHI’s mandate has serious gaps in coverage which may result in consumers not being able to have part of their complaint resolved by any ombudsman.

We have also noted in our letters to FSCO that there is a dearth of information from OLHI about the types of complaints they receive and deal with (for example, there is no information provided on the number of segregated fund complaints in their 2014 Annual Report), and that consumers likely have little awareness of OLHI.

FSCO should work with other regulators and ombudservices to provide a single point of entry for a financial consumer’s complaint so that they do not have to navigate on their own through the regulatory labyrinth in order to have their concern addressed. The individual’s complaint should be guided to the appropriate place for resolution by intake staff trained specifically for this purpose rather than the consumer being sent away to another place where their complaint may or may not be addressed.

II. Whether FSCO is Carrying out the Activities and Operations as Required in its Mandate

The recent Auditor General’s Report and the 2014 IMF Report indicate that FSCO is not adequately fulfilling its mandate. There are serious issues with:

- (i) compliance with existing rules;
- (ii) a lack of enforcement by FSCO against agents who have been disciplined by another regulator;
- (iii) a lack of any proactive enforcement by FSCO;
- (iv) inadequate investigations by FSCO in response to a complaint; and
- (v) seriously inadequate complaint handling in response to a consumer complaint and, given the low awareness of where to complain, a relatively high incidence of complaints.⁹

FAIR Canada’s experience has been the following:

⁹ Office of the Auditor General of Ontario Audit Report, 2014, Chapter 3.03, at page 147-148, figure 11, which shows between 640 and 965 insurance complaints each year (from data for years 2010 to 2014 with 60% of those complaints relating to auto, property and casualty sectors, report available online at http://www.auditor.on.ca/en/reports_en/en14/303en14.pdf.

- (i) FSCO has been very slow to address a complaint;
- (ii) There is no proactive examination activity;
- (iii) The product suitability process has serious flaws and does not comply with international principles;
- (iv) Lack of oversight;
- (v) Lack of adequate enforcement when rules violated;
- (vi) Discipline by the MFDA or other SROs does not get addressed by FSCO and consumers are put at risk of harm as a result since delays and failures to handle, investigate or resolve complaints affects individuals who complain as well as consumers who continue to be “serviced” by the problematic agent;¹⁰ and
- (vii) Self-regulation through industry guidance is inadequate and insufficient and the policy-making process is unduly influenced by industry and industry associations such as CLHIA and Advocis without any adequate informed consumer voice being heard.

FAIR Canada recommends that the following recommendations from the IMF Report need to be addressed:

- (i) Review the adequacy of FSCO’s supervisory resources;
- (ii) Review whether FSCO should be subject to hiring controls set by the Ontario Public Service;
- (iii) Empower FSCO to issue enforceable rules on product development and promotion;

¹⁰ See our August 2011 Newsletter:

<http://archive.constantcontact.com/fs070/1102284477892/archive/1107399885184.html>. See also this more recent example: http://www.investmentexecutive.com/-/ontario-life-agent-handed-one-month-ban?redirect=http%3A%2F%2Fwww.investmentexecutive.com%2Fhome%3Bjsessionid%3DJL63fj1BW7uVX3WrNxulWWEP%3Fp_p_id%3D101_INSTANCE_7mNgPO2cLPES%26p_p_lifecycle%3D0%26p_p_state%3Dnormal%26p_p_mode%3Dview%26p_p_col_id%3Dcolumn-1%26p_p_col_pos%3D1%26p_p_col_count%3D3 and <http://www.fSCO.gov.on.ca/en/about/enforcement/enforcement-online/Documents/2014-mar-785-Harvey.html>.

- (iv) Empower FSCO to require¹¹ insurers and intermediaries to conduct needs analysis before providing advice and to meet policy servicing obligations; and
- (v) Review the adequacy of supervisory resources of FSCO for regulatory policy formulation and for carrying out proactive conduct of business supervision.

FAIR Canada also notes that voluntary codes of conduct do not provide adequate consumer protection. It is all very well to have a voluntary code of ethics that states you put the interests of the consumer first but if you oppose instituting a statutory best interest standard and act in a conflicted manner where you put your own interests (remuneration) before that of the consumer's (due to misaligned incentives), the code of ethics is simply misleading and not useful in practice.

III. Should FSCO's Activities Continue to be Performed by FSCO or Should Those Activities Be Performed by a Different Entity, including an SRO?

FAIR Canada's recommendations are as follows:

- (i) Any obvious expertise that exists elsewhere should be utilized to reduce the burden on FSCO's mandate. See section I(3) above wherein we recommend that OSFI and the OSC's expertise be utilized in respect of solvency regulation and segregated funds respectively. If insurance products that are like "investment products" cannot be transferred to the OSC to regulate, then the same legal framework for the regulation of such products should be adopted on the insurance side so that like products are regulated in a like manner;
- (ii) The governance framework for FSCO should be revised to meet international best practices and international standards and to ensure adequate transparency and accountability;
- (iii) FSCO needs to have adequate resources and needs to enhance its capabilities and expertise in the areas it regulates;
- (iv) Regulatory fragmentation should be lessened and not increased through any reforms;
- (v) The suggestion made by some stakeholders that the insurance council framework should be examined as a possible model to move towards needs to be looked at with a critical eye. We are unable to state whether an insurance council framework would provide any improvement since there is no publicly available data on the

¹¹ In FAIR Canada's opinion, this means the need for regulatory requirements rather than industry guidelines or principles.

level of consumer complaints, how often insurance councils audit insurance agents and whether their enforcement record is any better. Our understanding is that they are largely reactive in nature (i.e., respond to individual complaints in investigating agents rather than conduct proactive compliance and enforcement). The 2014 IMF Report did not examine any province with an insurance council model so we do not have an objective review of an insurance council's performance;

- (vi) Any model should not separate the regulation of dealers or insurers and managing general agencies from the regulation of its employees and agents (i.e., financial advisors). It is much more efficient and effective to have *one regulator* oversee both the entity and their employees and agents given the business models, compensation structures, and supervisory obligations, etc.; and
- (vii) We oppose Advocis' view that FSCO has served the interests of industry *and consumers* (our emphasis) well over the years and that an organization (such as Advocis) be delegated administrative authority to enforce professional standards and regulate the behaviour of financial advisors.

IV. Changes to the Current Governance Structure And Accountability Mechanisms

FAIR Canada recommends, in addition to the points raised in section III above, that:

- (i) The Regulatory powers of FSCO need to be amended so that it has rule-making authority;
- (ii) The adjudicative tribunal should have complete independence from the policy and regulatory division of FSCO by making it a separate entity. This would allow the independent adjudicative tribunal to function, and to be perceived, as fully independent of the regulatory agency and its investigative arm;
- (iii) The structure of other regulators in the financial services sector such as the Ontario Securities Commission and the Autorité des marchés financiers (the "AMF") with its Chambre de la securite financiere and the Chambre de l'assurance de dommages, should be reviewed and assessed when determining how to improve the governance structure of FSCO;
- (iv) There is a need for an interprovincial licensing system and automatic reciprocal enforcement of disciplinary orders by regulators (insurance or securities). Disciplinary action against an individual and/or a firm by any financial services regulator should automatically result in equivalent disciplinary action by FSCO against that individual and/or firm;

- (v) There is a need for a comprehensive national database that is user-friendly to assist Canadian consumers in checking the registration and disciplinary history of any person or firm who offers investment advice, whether that advice comes from someone in the insurance regulated sector, securities regulated sector or the banking sector; and
- (vi) The regulator should be adequately funded by the industry it regulates so that it can attract talented individuals through competitive compensation and so that it can have an organizational culture that attracts highly motivated staff.

V. Future of the Financial Services Sector

FAIR Canada believes the following trends will likely have significant impact on financial services regulation:

- (i) The increasing complexity of financial products and increasing convergence between products offered in the insurance and securities sector¹²;
- (ii) Increasing technological change will impact how consumers buy (or are sold) financial products;
- (iii) Aging demographic;
- (iv) Increasing self-reliance in saving for retirement;
- (v) Low interest rate environment and low economic growth;
- (vi) Increasing demand for income-producing products;
- (vii) Increasing number of companies that sell products from all the regulatory sectors – banking, securities and insurance;
- (viii) Increasing number of investment products aimed at financial consumers who are not sophisticated in financial matters and have low financial literacy;
- (ix) Increasing debt levels of consumers; and

¹² FAIR Canada letter to FSCO dated June 6, 2011 at page 5, footnote 2.

- (x) The age of retirement often not being chosen by the individual but forced upon them through circumstances beyond their control (with health being a major reason).¹³

FAIR Canada believes that the following is urgently needed:

- (i) A regulatory regime that oversees whether the products being sold to consumers meet their needs and are in their best interests;**
- (ii) Consistent treatment of consumers across the regulatory spectrum;**
- (iii) An adequately funded and informed consumer voice that is part of the policy-making process; and**
- (iv) A statutory best interest standard applicable whenever financial advice is provided to consumers.**

We hope that our comments are helpful to the Panel's work and would be happy to answer any further questions the Panel may have. Please contact Neil Gross at 416-214-3408 (neil.gross@faircanada.ca) or Marian Passmore at 416-214-3441 (marian.passmore@faircanada.ca).

Sincerely,



Canadian Foundation for Advancement of Investor Rights

Cc: George Cooke
James Daw
Lawrence Ritchie

¹³ <http://www.theglobeandmail.com/globe-investor/personal-finance/retirement-rrsps/nearly-half-of-canadians-forced-to-retire-earlier-than-planned-poll-shows/article25219041/>